

Audit report

**AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL
LEGISLATURE AND THE COUNCIL ON MAKHUDUTHAMAGA LOCAL MUNICIPALITY**

30 November 2010

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REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Makhuthamaga Municipality, which comprise statement of financial position as at 30 June 2010, and the statement of financial performance, statement of changes in net assets, cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information as set out on pages xx to xx.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of General Recognised Accounting Practice (SA Standards of GRAP) and in the manner required by the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA). This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of South Africa and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004), my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 1570 of 2009*, issued in *Government Gazette No. 32758 of 27 November 2009*. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Basis of accounting and framework

4. The municipality converted from the Institute of Municipal Finance Officers (IMFO) basis of accounting to SA Standards of GRAP with effect from 1 July 2009. The conversion was done retrospectively to 1 July 2008. Although the conversion journals were submitted, I could not corroborate the journals with the amounts in the annual financial statements. Consequently, I was unable to confirm the occurrence, completeness, classification, accuracy, valuation, rights to and obligations in respect of, as well as the compliance of the balances disclosed in the annual financial statements for the years ended 30 June 2009 and 30 June 2010.

Property, plant and equipment

5. The accounting records of the municipality did not allow me to perform the required audit procedures to satisfy myself on the existence of property, plant and equipment amounting to R47 503 736 included in the financial statements. The municipality's records did not permit the application of alternative audit procedures.
6. The municipality could not provide sufficient appropriate audit evidence to support capital expenditure of R1 244 414. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that assets additions occurred, were accurate and properly recorded. Consequently, I did not obtain sufficient appropriate audit evidence to

satisfy myself as to the occurrence, completeness, accuracy, cut-off and classification of assets additions of R58 482 231.

7. An adjustment amounting to R2 567 479 was made to the infrastructure balance of R141 980 807 in note three of the financial statements. Documentation supporting this adjustment could not be provided by the municipality.

Revenue

8. There was no system of control over traffic revenue on which I could rely on for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all traffic revenue was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of traffic revenue of R3 092 455. The entity's records did not permit the application of alternative audit procedures regarding the revenue.
9. The municipality could not provide sufficient appropriate audit evidence to support an amount of R633 998 included in traffic revenue. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the occurrence, accuracy, cut-off and classification of this amount included in traffic revenue.
10. There was no system of control over property rates revenue on which I could rely for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all property rates revenue was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of property rates revenue amounting to R17 956 005.
11. There is also an explained difference of R3 607 477 between the amount disclosed in the financial statements and my recalculated amount of R21 563 482. Consequently, I was unable to satisfy myself as to the accuracy of property rates revenue of R17 956 005 in the statement of financial performance.

Expenditure

12. The municipality could not provide sufficient appropriate audit evidence to support expenditure of R3 006 005 for expenditure. There was no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that expenditure occurred, were accurate and properly recorded. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the occurrence, completeness, accuracy, cut-off and classification of expenditure of R52 896 708.00.

Valued Added Tax (VAT)

13. The municipality could not provide sufficient appropriate audit evidence to support the balance of R11 017 602 as disclosed in note six to the financial statements. As a result, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the valuation and allocation, rights and existence of the VAT balance in the financial statements. The municipality's records did not permit the application of alternative audit procedures regarding the receivable balance.

Trade and other payables

14. The municipality could not provide sufficient appropriate audit evidence to support an amount of R3 128 089 included in the balance of R5 865 883 in note 10 to the financial statements. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the existence, rights, completeness, and valuation of trade payables.

15. There was no system of control over leave on which I could rely for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that provision for leave was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, rights and obligations, existence and valuation of provision for leave of R811 234.00.

Unauthorised expenditure

16. Unauthorised expenditure to the amount of R2 406 070 was incurred due to the utilisation of the municipal infrastructure grant allocation for expenditure incurred in respect of the municipal structure infrastructure grant that is in contravention with section 38 of the Division of Revenue Act, No 12 of 2009 (DoRA). The unauthorised expenditure was not disclosed in the financial statements as required by section 125(2) (d) (i) of the MFMA.

Disclaimer of opinion

17. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matters

18. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of corresponding figures

19. As disclosed in note 28 to the financial statements, the corresponding figures for the year ended 30 June 2009 have been restated as a result of errors discovered during 2010 in the financial statements of the municipality at, and for the year ended, 30 June 2009.

Fruitless and wasteful expenditure

20. As disclosed in note 32 to the financial statements, fruitless and wasteful expenditure to the amount of R4 304 was incurred on late payments to suppliers.

Additional matters

21. I draw attention to the following matter. My opinion is not modified in respect of these matters:

Unaudited supplementary schedules

22. The supplementary information as set out on page xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

23. As required by the PAA and in terms of *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the following key laws and regulations and financial management (internal control).

Predetermined objectives

24. Material findings on the report on predetermined objectives, as set out on pages xx to xx, are reported below:

Non-compliance with regulatory and reporting requirements

No reporting against predetermined objectives, indicators and targets

25. The municipality did not prepare the annual performance report in terms of section 46 of the MSA, and section 121(3)(c) of the MFMA.

Lack of adoption or implementation of a performance management system

26. The municipality did not implement a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players, as required in terms of sections 36, 38 and 41(2) of the MSA, and regulations 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

Compliance with laws and regulations

MFMA

The audit committee was not properly established

27. Contrary to section 166(1) MFMA the municipality did not have an audit committee.

The internal audit function was not established

28. Contrary to section 165 of MFMA the municipality did not establish an internal audit function.

Expenditure incurred was made in vain or could have been avoided resulting in fruitless and wasteful expenditure

29. Contrary to section 62 of MFMA the municipality incurred fruitless and wasteful expenditure.

Expenditure was not paid within the parameters set by the applicable legislation

30. Contrary to section 65(2) (e) of the MFMA the municipality did not pay for expenditure within the required 30 days from receipt of the invoice from suppliers.

The financial statements were not prepared in accordance with applicable legislation

31. Contrary to section 122(1) of the MFMA the municipality did not prepare financial statements that fairly present its state of affairs as material misstatements were corrected during the audit.

The accounting officer did not adhere to his statutory responsibilities

32. Contrary to section 62(1)(d) of the MFMA the accounting officer did not comply with his legislative responsibilities to implement effective, efficient and transparent processes of financial and risk management to prevent and detect unauthorised expenditure and fruitless and wasteful expenditure.

Municipal Systems Act of South Africa, No. 32 of 2000 (MSA)

The municipality did not implement a performance management system

33. Contrary to section 57 of the MSA the municipality has not implemented a performance management system.

Councillors did not declare their financial interest

34. Contrary to schedule 1 section 7 of the MSA the councillors did not declare their financial interest.

SCM officials and other role players did not declare rewards

35. Contrary to sec 46(2)(e) of the SCM regulations the municipality did not implement controls for SCM officials or other role players to declare any reward, gift, hospitality or any other

- benefit promised, offered or granted to that person or to any close family member, partner or associate of the person.

INTERNAL CONTROL

36. I considered internal control relevant to my audit of the financial statements and the report on predetermined objectives as well as compliance with the MFMA and MSA, but not for the purpose of expressing an opinion on the effectiveness of internal control.
37. The matters reported below are limited to the significant deficiencies regarding the basis for qualified opinion paragraph, the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

- **Leadership**

- Tone at the top*

- Management's philosophy and operating style does not promote effective control over reporting.

- Quality is not understood by all to be a prerequisite and is not embedded in the entity's values

- Performance is not measured

- Oversight responsibility*

- The accounting officer does not exercise oversight responsibility over reporting and compliance with laws and regulations and internal control. As a result, the financial statements were subject to material amendments resulting from the audit and non-compliance issues were noted.

- Human resource policies do not facilitate the training and disciplining of personnel.

- Key officials were not available during the audit

- The accounting officer does not evaluate whether management has implemented effective internal controls by gaining an understanding of how senior management has met its responsibilities.

- **Financial and performance management**

- Quality, reliable financial statements and management information*

- The financial statements and other information to be included in the annual report are not reviewed for completeness and accuracy prior to submission for audit.

- The financial statements were subject to material amendments resulting from the audit.

- Pertinent information is not identified and captured in a form and time frame to support financial and performance reporting.

- Proper record keeping and record management*

- Requested information was not available and supplied without any significant delay.

- Adequate financial management systems*

- General information technology controls are not designed to maintain the integrity of the information systems and the security of the data.

- **Governance**

- Risk identification and management*

- The entity does not have a formal risk assessment process.

- The entity does not identify risks relating to the achievement of financial and performance reporting objectives.

The risk of material misstatement due to fraud is not considered.

Internal controls are not selected and developed to prevent and correct material misstatements in financial reporting and reporting on predetermined objectives.

Fraud prevention, detection and response

A fraud prevention plan is not documented and used as per the requirements of applicable legislation.

Auditor-General
Polokwane

30 November 2010



AUDITOR-GENERAL
SOUTH AFRICA

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